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ADOPTION OF THE REPORT OF THE COMMISSION ON ITS SEVENTEENTH SESSION

Draft report

Addendum

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Chapter ___

ROLE OF TRANSNATIONAL CORPORATIONS IN SERVICES, INCLUDING TRANSBORDER DATA FLOWS

1. The Commission considered agenda item 5 at its 6th meeting, on 12 April 1991. It had before it the reports of the Secretary-General on transnational banks and the external indebtedness of developing countries (E/C.10/1991/4), transnational banks and debt-equity conversions (E/C.10/1991/5) and the impact of transnational service corporations on developing countries (E/C.10/1991/6).

A. Role of transnational banks

2. In introducing the item, the Executive Director observed that the problem of debt remained serious for developing countries. Only five debtor countries had so far succeeded in concluding debt structuring agreements with transnational banks. Negative net transfers from highly indebted developing countries due to commercial debt continued to increase and there had been no significant improvement in interest-to-export ratios for most debtor countries. Nevertheless, there was a decline in commercial bank claims for 18 indebted countries to the tune of $45 billion over a period of 1987-1990. To some extent, this reduction had been facilitated by regulatory changes in creditor countries. The Executive Director drew the attention of the

Commission to areas for further improvement in regulatory frameworks contained in the report, and, in particular, to those concerning modifications in capital guidelines, tax relief in discounted asset sales, and accounting penalties for banks which refused to participate in debt reduction agreements. He also emphasized the need for closer coordination among creditor countries in formulating regulatory changes and for a stronger political commitment on their part to debt reduction.

3. Turning then to the issue of debt-equity swaps, the Executive Director pointed out that debt-equity swaps had nearly doubled to $9 billion in 1990 compared to their level in 1989. Developing debtor countries had implemented debt-equity swap programmes both as a means of debt reduction and to achieve a number of other development objectives. Among these were stimulation of foreign investment, support to programmes of privatization of State enterprises, avoidance of round tripping and mitigation of inflationary pressures.

4. Reviewing the experience of several countries, the Executive Director observed that the cumulative effect on debt reduction due to debt-equity swaps had been relatively small in relation to the volume of debt in most countries. The experience in respect of fulfilment of other objectives was mixed. However, it had functioned as a major vehicle for foreign direct investment, though it was difficult to estimate the extent of additionality. He concluded by stating that there were inherent trade-offs in the implementation of debt-equity swap programmes which had to be structured carefully to suit a country's priorities. Moreover, debt-equity swaps could not obviate the need for implementing other means of debt reduction, including write-offs.

5. Most delegations pointed out that the problem of debt continued to pose a constraint to the growth and development of developing countries. They endorsed the view expressed in the report that there was no ground for complacency with respect to the debt owed to the transnational banks by developing countries. Huge transfers to those banks exacerbated the already precarious financial situation of developing countries. Though it marked an important step towards the solution of debt problems, the Brady plan was complex and involved protracted negotiations. It was not, therefore, surprising that the number of countries that had benefited from the plan was very limited and the volume of debt reduced was low.

6. It was observed that the success of seemingly minor regulatory changes in reducing transnational bank debt clearly showed that Governments of creditor countries were not powerless in influencing transnational bank decisions and hence their cooperation was essential for the reduction of developing countries' debt. This underscored the need for further pursuit of regulatory changes in creditor countries in a coordinated manner in order to facilitate speedier debt reduction; developed countries had to show leadership in creating the necessary policy framework.

7. With regard to debt-equity swaps, the delegations that expressed themselves on the subject were of the view that debt-equity swaps opened a new avenue of debt reduction. However, it could not be considered to be a substitute for other measures. There were both positive and negative consequences of debt-equity swaps for countries that had implemented such programmes and hence those programmes needed to be structured carefully. Cumbersome regulations should be avoided and suitable macroeconomic policies could help mitigate some negative consequences.

8. Two delegations expressed the view that the subject of debt did not fall within the mandate of the Centre.

9. Some delegations offered suggestions for further work by the Centre in relation to transnational banks. These included examination of the positive contribution of transnational banks to host developing countries; and analysis of the interface between debt, privatization, debt-equity swaps and foreign direct investment as a package.

Action taken by the Commission

10. The Commission took note of the reports of the Secretary-General on transnational banks (E/C.10/1991/4 and E/C.10/1991/5) and requested the Centre to continue further work in the light of the discussions at the seventeenth session.

B. Role of transnational corporations in other services

11. In introducing the item, the Executive Director of the Centre stated that the report focused on the impact of transnational service corporations on competition and market structure, the provision of unique services and the socio-cultural aspects of host countries. He drew attention to the emphasis being placed by developing countries on increasing the competitiveness and efficiency of their services sectors, particularly of their infrastructure and producer services. In that connection, many developing countries were more inclined than in the past to permit transnational corporations to play a role in upgrading their service industries. The important question was whether, to what extent and how, transnational corporations could contribute to greater efficiency, greater availability, improved quality, or lower prices for services. That depended on many factors, including government policies concerning competition, the nature of the industry and the behaviour of transnational service corporations. Host country policies encouraging market entry by local firms as well as foreign investors were important if transnational corporations were to promote competition and efficiency rather than capture monopoly rents. In financial services, it would be necessary to ensure that the process of deregulation and restructuring for greater competitiveness did not conflict with basic prudential requirements for financial stability and consumer protection. In capital-intensive services (such as telecommunications), the role of transnational corporations would be

to inject capital and technology rather than enhance competition, except in certain market segments of the industry. In some other services, such as accounting or engineering, transnational corporations often chose to specialize in sophisticated services in which they had comparative advantage in terms of quality, rather than compete directly with local companies. Finally, the provision of unique services was a contribution that transnational corporation affiliates made to a majority of developing countries, because even the most restrictive of countries permitted operations of transnational corporations to provide services that, being untradable, could not otherwise be obtained. Countries wishing to use service affiliates in their competitive function would, however, have to reconsider regulations restricting transnational corporations to the provision of unique services.

12. The Executive Director also drew attention to the social and cultural influences of transnational service corporations in host developing countries and the considerations underlying government policies in that regard. Some of the obvious undesirable socio-cultural costs might be minimized by appropriate policies and actions of Governments as well as transnational corporations. In the most sensitive cases, however, Governments and societies had to determine the trade-offs between economic benefits and socio-cultural costs of the activities of foreign service affiliates.

13. Most delegations agreed that issues relating to increasing the efficiency and competitiveness of the services sectors in both developed and developing countries were becoming increasingly important in view of the high share of the service sector in gross national product and of the interlinkages of producer services to other sectors of the economy. Many delegations welcomed the revision of the policy objectives in selected producer services in many developing countries towards the promotion of greater availability and improved quality of services, including, among others, moving tentatively towards lifting restrictions on transnational corporations. They agreed that transnational service corporations could play a critical and beneficial role in helping build up and improve the efficiency of service industries in developing countries and that competition was the best tool for increasing the efficiency in many, though perhaps not all, service industries. One delegation noted that far more efforts were needed to increase competition in still heavily regulated and protected service sectors. Another delegation suggested that liberalization of service industries fostered competition and maximized the benefits of foreign investments.

14. Several delegations agreed that some of the impacts of transnational service corporations on the social and cultural fabric of host countries might be potentially negative. One delegation supported the conclusions of the report that trade-offs between positive and potentially negative effects were often difficult to identify and that they depended largely on the definition of what Governments and societies considered costs and benefits. While one delegation acknowledged the increasingly positive contributions of transnational service corporations to host developing countries and noted that the corporations were increasingly welcome in those countries, it pointed out, at the same time, that service industries in most developing countries could

not yet compete on equal terms with transnational service corporations. Therefore, it suggested that international frameworks on transactions in services should include preferences for developing countries, especially in labour-intensive services. The code of conduct would be a desirable addition to any rules on trade in services, the continuing absence of which was not beneficial for the expansion of international trade in services. Developing countries should more closely monitor restrictive business practices by transnational corporations to minimize negative effects related to those practices.

15. Some delegations drew attention to the role of transnational service corporations in the transition process of their countries towards market economies. They were of the view that lack of services in their economies hampered progress in other sectors and inflows of foreign direct investment. They agreed that transnational corporations accelerated the process of acquisition of crucial services and were, therefore, generally welcomed in countries in transition. There was, however, the awareness that transnational corporations alone could not build the service sector in those countries. Domestic effort, including education and increased investment in infrastructural services, was hence needed to close the development gap in service industries.

16. All delegations that spoke stressed the importance of the Centre's research in the area of foreign direct investment and transnational corporations in services. In particular, they emphasized the need for policy-oriented studies on the impact and implications for countries, particularly developing ones, of the liberalization of foreign direct investment and trade in services, focusing especially on ways and means of increasing the efficiency and competitiveness of infrastructure and producer services and the role of transnational corporations. In that context, they welcomed efforts aimed at closer coordination of work between the Centre and the United Nations Conference on Trade and Development (UNCTAD) and stressed that such efforts should continue, including those with other concerned agencies such as the General Agreement on Tariffs and Trade (GATT), the World Bank and the Organisation for Economic Co-operation and Development (OECD). Other areas that warranted research were tradability of services and the role of transnational corporations in the development of the services sector in developing countries, including that in the establishment of international service centres and the transfer of technology in services. It was also suggested that the Centre extend its research to issues relating to the role of transnational service corporations in the countries in transition. Delegations also supported the Centre's technical assistance efforts in the area of services, with particular focus on helping developing countries and countries in transition to review their existing policy framework concerning foreign direct investment and transnational corporations in services.

Action taken by the Commission

17. The Commission took note of the report of the Secretary-General on the impact of transnational service corporations on developing countries (E/C.10/1991/6). It requested the Secretary-General to conduct further in-depth research and technical cooperation in the area of services, taking into account the deliberations of the Commission, and to submit a report thereon to the Commission at its eighteenth session.